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MISSOURI PACIFIC RAILROAD ANNUAL REPORT 1968

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President, Central Missouri Trust Co., Jefferson City

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President, Missouri Pacific Railroad Company and The Texas and Pacific Railway Company, St. Louis

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Retired, St. Louis

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Senior Vice President and Director Mississippi River Corp.; President, River Corp., St. Louis

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Chairman of the Board and President, Mississippi River Corp.
Chairman of the Board, Missouri Pacific Railroad, St. Louis

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Estate Management and Corporate Executive, New York

J. T. SUGGS
Chairman of the Board
The Texas and Pacific Railway Company, Dallas

†RAYMOND V. TERRY
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Mississippi River Corp.
President, Mississippi River Transmission Corp., St. Louis

*Executive Committee;
†Finance Committee;
**Chairman of Executive Committee;
††Chairman of Finance Committee.

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President, St. Louis

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Executive Vice President, St. Louis

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Senior Vice President, St. Louis

M. M. HENNELLY
Vice President and General Counsel, St. Louis

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Vice President, Dallas, Texas

T. D. RODMAN
Controller, St. Louis

L. A. BRUNS
Treasurer, St. Louis

C. A. ROCKWELL
Secretary, St. Louis

*Effective Feb. 1, 1969

MISSOURI
PACIFIC
RAILROAD
COMPANY

Transfer Agents

UNITED STATES TRUST COMPANY OF NEW YORK
Transfer Agent
Class A Stock, 45 Wall Street
New York, N. Y. 10005

THE BOATMEN'S NATIONAL BANK OF ST. LOUIS
St. Louis Transfer Agent
Class A and B Stock, 300 No. Broadway
St. Louis, Mo. 63102

Registrars

MANUFACTURERS HANOVER TRUST COMPANY
Registrar
Class A Stock, One Whitehall Street
New York, N. Y. 10015

ST. LOUIS UNION TRUST COMPANY
St. Louis Registrar
Class A and B Stock, 510 Locust Street
St. Louis, Mo. 63101

Annual Meeting of Stockholders
The Second Tuesday in May
General Offices
Missouri Pacific Building
St. Louis, Mo. 63103

Missouri Pacific System

Annual Report for the year ended December 31, 1968

Consolidated Financial and Operating Highlights

Income and Expense Items	1968	1967
Operating Revenues	$445,749,000	$424,192,000
Operating Expenses	350,612,000	325,750,000
Operating Ratio (Rail Line)	76.0%	74.0%
Income Available for Fixed Charges	53,608,000	59,443,000
Times Fixed Interest Earned	2.3	2.7
Net Income Before Extraordinary Items —		
In Conformity with I.C.C. Accounting Principles	19,418,000	23,281,000
Adjusted to Generally Accepted Accounting Principles	11,791,000	17,223,000
Extraordinary Items	2,941,000	8,200,000
Net Income (Including Extraordinary Items) —		
In Conformity with I.C.C. Accounting Principles	22,359,000	31,481,000
Adjusted to Generally Accepted Accounting Principles	14,732,000	25,423,000
Cash Dividends per Share — Class A and B Stocks	5.00	5.00
See Page 12 for Information Relating to the Class A and Class B Capital Stocks of the Company		
Financial Position		
Gross Capital Expenditures	$ 59,921,000	$ 66,579,000
Depreciation and Retirements Charged to Income	35,915,000	32,551,000
Working Capital	26,689,000	35,504,000
Long Term Debt, including amount due within one year	717,452,000	714,434,000
Freight Statistics		
Average Miles of Railroad Operated	11,463	11,541
Revenue Ton Miles (1,000's)	31,619,138	30,780,968
Revenue per Ton Mile (cents)	1.25	1.20
Employees		
Total Amount of Payroll	$190,350,000	$182,940,000
Average Annual Wages	8,668	8,109
Average Number of Employees	21,959	22,559

To Our Stockholders:

Net income for the Missouri Pacific System dipped during 1968 despite improved performance in a number of important areas such as gross revenues, revenue ton-miles, operating efficiency and new business.

The reason for this disparity between performance and result is clear. It is simply that the growth in business and revenue was not as sharp as the surge in the cost of doing business. A modest freight rate increase, granted only after protracted hearings and lengthy delays, did not offset wage increases averaging 6 per cent, an 8 per cent rise in materials costs and other increased expenses. Nor will the existing rate increases be enough to make up for even higher wage and materials costs anticipated during 1969. Despite successes in numerous areas, the railroad industry enters 1969 with one of the lowest returns on investment in the entire economic sphere.

Consolidated net income before extraordinary items of the Missouri Pacific System, on the basis of Interstate Commerce Commission accounting principles, was $19,418,000, a decrease of $3,863,000 from that of the previous year. With non-recurring extraordinary income added, the consolidated net income figure was $22,359,000 in 1968 as compared with $31,481,000 in 1967. Missouri Pacific's 1968 extraordinary income of $2,941,000 after taxes is the result of a change in accounting methods prescribed by the Interstate Commerce Commission.

Operating revenues for the year were $445,749,000, an increase of $21,557,000 over 1967. Operating expenses of $350,612,000 were $24,862,000 above those of the earlier year. For the fifth consecutive year, all stockholders received a cash dividend of $5 per share.

Despite some adverse influences, freight revenue for 1968 rose 7.1 per cent. Adverse factors included a strike on our lines during February, work stoppages among a number of important industries we serve and a decline in export grain shipments caused by sharply depressed prices. On the positive side, industrial activity continued on a higher level than during 1967. Also, by providing modern, high-capacity equipment and by offering attractive incentive pricing, we were able to encourage heavier loadings of manufactured goods and other products.

By continuing a large-scale capital improvements program during 1968 we were able to purchase the cars and locomotives and build the modern facilities necessary to attract more revenue and partially off-set higher costs by operating with greater efficiency. We spent $59,921,000 during 1968 and have budgeted another $51,154,000 for capital improvements during 1969. For the period 1961 through 1969, MoPac will have spent in excess of $500,000,000 on physical improvements and fleet additions in an effort to construct a modern transportation system.

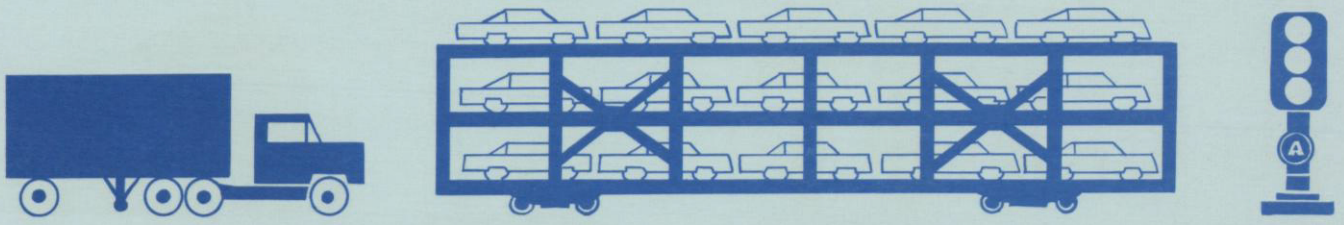
This physical upgrading of the system has been accompanied by a continuing series of improvements in services, pricing and marketing innovations and management controls which are no less important to the company's long range goals.

Industrial development continued in 1968 with 201 new or expanded industries, representing a capital investment of $377,564,344, locating along our lines. During the past five years, approximately 1,400 new or expanded industries, representing a capital investment of $2,000,000,000, have been established along the Missouri Pacific System. New industries such as these will contribute substantially to future growth in traffic and revenues.

Financial and Corporate

At December 31, 1968, our consolidated cash and temporary cash investment position amounted to $39,861,000 as compared to $58,260,000 at December 31, 1967, or a decrease of $18,399,000. Working capital likewise shows a decrease of $8,815,000 from $35,504,000 at December 31, 1967 to $26,689,000 at the end of 1968.

It was during August 1968, pursuant to an Exchange



Offer, that our investment in Atchison, Topeka & Santa Fe Railway Company, 5% Preferred Stock was converted to $29,644,000 principal amount of Santa Fe Industries Inc. 6¼% Convertible Subordinated Debentures. During the year funds were used, among other things, to increase our ownership in the Chicago & Eastern Illinois Railroad, acquire a fifty per cent equity in the Alton & Southern Railway, and reduce our outstanding mortgage debt.

Consolidated funded debt, including debt due within one year, was $717,452,000 at year end as compared with $714,434,000 at December 31, 1967. Equipment obligations issued during the year totaled $31,194,000 while repayments amounted to $22,614,000, resulting in an increase of $8,580,000.

Intermodal Services

Missouri Pacific is committed to the long-term goal of operating as a total transportation and distribution company. We believe full development of this concept would enable MoPac to expand its transportation capacity most efficiently and economically and would result in lower transportation costs to the shipper with corresponding savings to the consumer. During 1968, we advanced further toward this total transportation goal. Following is a recap of our progress in this area, including existing operations as well as proposed ones.

Trucking Operations

Missouri Pacific Truck Lines, Inc., and The Texas and Pacific Motor Transport Company, both wholly owned subsidiaries with 16,800 certificated miles, continued to make gains in all phases of their operations.

Gross revenues from these companies in 1968 amounted to $20,666,000, an increase of $2,006,000 over 1967. Net income of $570,000 was slightly below that of 1967 because of increased labor costs and a delay in adjusting freight rates.

The motor and trailer-on-flat-car equipment fleet was expanded during 1968 by the addition of 150 power units and 202 new trailers. An additional 169 power units and 134 new trailers are to be purchased during 1969. These additions will provide our fleets with 3,800 units of highway equipment.

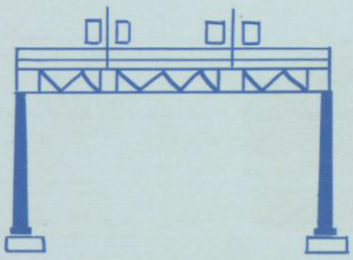
Historically, our truck lines have been required to operate under uneconomical, artificial and antiquated restrictions imposed by regulatory bodies because of rail ownership. Substantial progress was made during 1968 in eliminating some restrictions, but even greater progress must be made if we are to serve more small package patrons in smaller communities throughout our system.

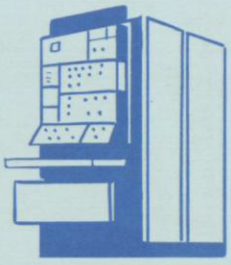
Piggyback

Piggyback, the now well established truck-rail combination, continued its rapid growth rate during 1968 with volume on the Missouri Pacific soaring 26 per cent above the previous year. The average gain, nationally, was less than 11 per cent.

A fleet of fast piggyback trains, construction and continued improvement of piggyback facilities and aggressive sales efforts are responsible for this above-average growth rate. MoPac's "Texas Piggyback Special" between St. Louis and Texas points, for example, averaged 80 trailers per day in 1968 compared to 70 in 1967 and 52 trailers per day in 1966. In addition, expedited piggyback trains were put into service during the year between Chicago and Houston-Ft. Worth in both directions and between Houston-Ft. Worth and St. Louis. Piggyback traffic also is commonly included in other fast trains on the system.

Piggyback facilities were constructed or expanded at Dupo, Ill., Corpus Christi, Longview and Odessa, Texas, and merchandise freight terminals were constructed at Bastrop and Lake Charles, Louisiana. A freight terminal at Odessa will open early in 1969. A consolidated piggyback and freight terminal facility will be constructed in two phases at Memphis, Tenn., with work to begin in 1969. Piggyback facilities also will be expanded at Kansas City while terminal operations at Addis and Anchorage, Louisiana, will be consolidated into a single operation at Addis.





Containerization

A study of containerization was completed in 1968 to determine traffic potential and future Missouri Pacific policy in this area. As a result of the study, a Traffic Manager-Containerization was appointed to devote full time to container traffic sales, research and development of new container markets, including rail-water and rail-air service.

During the year, 26 interchange agreements were negotiated with steamship companies and other container owners. A container pool was established at Dallas to provide better service to our customers. All-purpose flat cars, capable of handling either containers or wheeled trailers, were acquired. We also handled numerous movements of container traffic.

Missouri Pacific became a participating line in a Land Bridge tariff as a bridge carrier between the East and West Coast ports, pending actual materialization of such a service. The Land Bridge would use railroads as vital land links in intercontinental traffic. We expect containerization and intermodal interchange to grow at an accelerating rate in 1969.

Missouri Pacific Intermodal Transport, Inc.

Missouri Pacific Intermodal Transport, Inc., incorporated in Missouri in October, 1968, filed a tariff with the Federal Maritime Commission to serve as a non-vessel operator by water.

This new company will operate as a wholly-owned subsidiary of Missouri Pacific Truck Lines to handle documentation and arrange through container rates and service between the United States and foreign cities. It would use rail, highway and independent ocean services. This will simplify development and handling of containerized traffic between Missouri Pacific System territory and foreign points while contributing to the land bridge concept.

Missouri Pacific Airfreight, Inc.

Missouri Pacific Airfreight, Inc., incorporated in Missouri in December, 1967, filed an application in January with the Civil Aeronautics Board to operate as an airfreight forwarder. The application is still pending.

It is proposed that the new company offer air forwarder service between all stations on the Missouri Pacific System and all national and international points. This air freight service company would operate as a wholly-owned subsidiary of Missouri Pacific Truck Lines and would utilize system rail or motor service to or beyond commercial air terminals with all air transportation performed through contracts with existing airlines.

Air freight would enable Missouri Pacific to increase its range of services to shippers and communities, especially to those not having nearby air freight or container facilities.

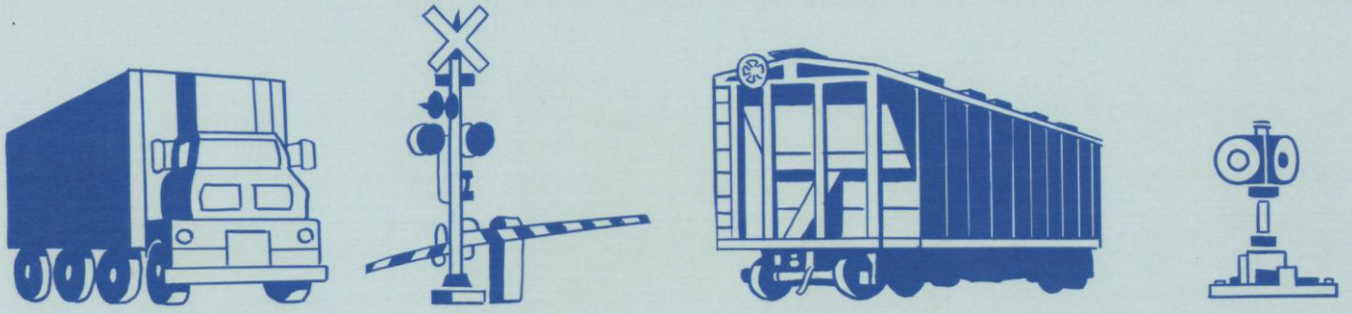
Services and Marketing

Further progress was made during 1968 in improving service, developing competitive pricing and performing market research in a number of areas. The overall aim is to provide as broad and competitive a range of services as possible to the shipper.

Pricing

Major activities in freight pricing were primarily concentrated on grain and chemical traffic. Important revisions in grain rates, particularly for export through Gulf ports, have been made to counter barge and truck-barge competition. Numerous volume rates were established on chemicals, with annual shipping minimums ranging from 37,500 to 90,000 tons.

Noteworthy in the area of liquid chemical traffic was the economic and engineering research which resulted in introduction of rates based on the use of eight-axle tank cars. This produced increased capacity by as much as 200,000 lbs. per car. Glycols and other high density chemicals are particularly adapted to this type of car. Advantages include lower rates to the shipper, decreased car mileage costs and higher net for the railroad.



Sulphur rates at minimum annual volumes of from 40,000 to 160,000 tons have been provided from West Texas origins to Florida and other points in the Southeast.

Rates have been successfully adjusted on other commodities too numerous to mention in order to secure traffic moving via other modes of transportation and to prevent diversion from the railroad.

Schedules and Service

Two new through freight trains were initiated in both directions between Chicago and North Little Rock. Service was improved as a result of eliminating handling of this traffic through the St. Louis Gateway, minimizing switching and improving both car and trailer utilization. Chemical traffic originating on the Kingsville Division, an area roughly running along the Gulf Coast between Houston and Brownsville, now is being handled more quickly by bypassing Settegast Yard in Houston.

Considerable progress was made in setting up cooperative switching arrangements with several railroads through the Memphis and New Orleans gateways. Missouri Pacific pre-blocks cars for delivery at destinations along the lines of the cooperating railroad while the other railroad does the same thing for MoPac. This has reduced switching time and eliminated congestion problems at these gateways. Our Terminal Car Control system was extended to the North Little Rock terminal during 1968, and will be installed at other points during 1969.

Five mobile agency routes were established in three states with headquarters at Harlingen, McAllen and Pharr, Texas; Alexandria, Louisiana, and Hobbs, New Mexico. Applications are pending for extension of this service which uses a series of mobile offices, linked by radio to the area headquarters, to transact a full range of transportation services right at the shipper's place of business. Two routes were authorized on a trial basis in Missouri in January, 1969.

Management Information Division

During the year, a lengthy study was completed of a complex, computer-oriented management information system. Approval was given for a start on the project and a Management Information Division, representing the skills of all major departments, was established under the Operating Department. The Missouri Pacific is well underway in development of an extensive program that will improve service and control of transportation operations. It is being put into effect gradually and will be complete in 1972.

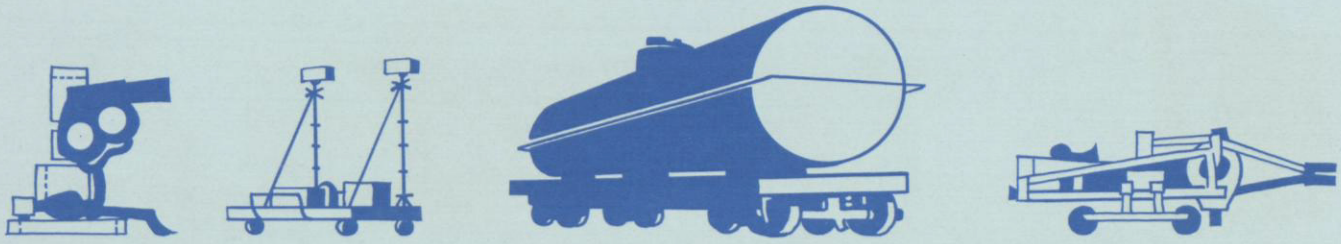
Among the features of the MIS program are:

- Establishment of Customer Service Centers at 45 locations where all business between the railroad and its customers can be handled at one spot. A successful pilot center has been opened at North Little Rock.
- Use of computers to choose the best routing for each car moving on the system, including selection of the proper train and establishment of switching orders for the car.
- Maintenance of a complete record on the availability, suitability and condition of each car.
- Automatic matching of car supply and car demand.

In line with the MIS system, a Transportation Control Center was installed at Missouri Pacific headquarters in St. Louis. There, car tracing for on-line and off-line traffic agencies is performed and car distribution for the Eastern District is centralized. Plans have been made to handle car distribution for the remainder of the System through this center. Numerous visitors toured this ultra-modern facility during the year.

Mail and Passenger Service

Mail, passenger and express revenue in 1968 declined $5,363,000 or 27.1 per cent. Fourteen passenger trains were discontinued, resulting in an annual saving of $2,294,000 and 1,806,000 less train miles. Decisions on proposed discontinuances of six additional passenger trains, aggregating 518,300 train miles and losses of $1,221,000, have not been announced by the appropriate regulatory agencies. Applications have been filed to discontinue four passenger trains totaling



560,000 train miles per year. All sleeping car service was discontinued December 31, 1968.

Capital Improvements

Innovations in marketing and services have been accompanied by a continuing program of maintenance and modernization of Missouri Pacific's physical facilities, track and fleet. The 1968 capital improvements program totaled $59,921,000.

Fleet purchases included 20 new diesel locomotives and 1,678 new freight cars, many of specialized design in order to meet the increasingly more specific needs of our customers. In addition, our own shop forces either rebuilt or converted for other uses a substantial number of cars.

Track Work

Among the largest physical improvement projects undertaken during 1968 were construction of a new branch line in West Texas, and a start on installation of a new and expanded yard at Fort Worth, Texas.

A 27-mile branch line was built from a point near San Martine, Texas, to the site of a new sulphur mining operation. Despite difficult working conditions, this project was completed in a record six months.

The Fort Worth project involves enlarging Lancaster Yard and converting it to an automated, electronic "hump" yard similar to existing yards at Kansas City and North Little Rock. This $5,500,000 project is scheduled for completion in 1970.

In addition, Missouri Pacific laid 181 miles of new and 117 miles of relay rail, nearly all of it continuous welded rail; renewed 1,120,900 cross ties; applied 1,110,000 cubic yards of ballast; surfaced 4,520 miles of track; restored embankment on 340 miles of track. MoPac also constructed 42 trestles totaling 11,801 lineal feet, most of them concrete structures, and installed eight steel spans totaling 653 lineal feet.

Numerous signals and communications projects were carried out during the year. Major projects included installation of 27.7 miles of CTC between Livonia and Addis, Louisiana and 13.3 miles of CTC in the Flinton, Illinois area. Eight radio base stations were installed as well as communication facilities for the terminal car control system at North Little Rock. Three more electronic in-motion track scales were put into service.

Shop Facilities

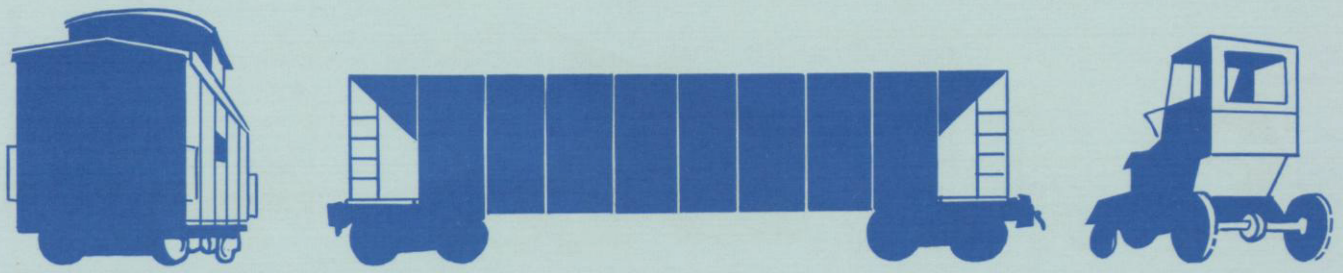
A new quick service diesel facility was completed at North Little Rock during 1968. An adjacent shop for heavier maintenance and repair will be built this year. A spot repair shop was built at Laredo, the busiest of our three gateways to the Republic of Mexico. A long-term modernization program at the heavy car repair and construction shops at DeSoto was completed with construction of a stripping building while an automatic diesel washing facility went into operation at Houston.

These projects were in addition to the terminal and piggyback facilities discussed under piggyback in this report.

Litigation and Control and Merger Cases

During 1968, the Chicago & Eastern Illinois Railroad, a newly acquired and substantial subsidiary of MoPac, in accordance with requirements of the ICC, negotiated a contract for the sale to the Louisville & Nashville Railroad of C&EI's line from Evansville to Chicago. The terms of this sale have been approved by the ICC and it is expected that the transaction will be consummated promptly in 1969. The remaining portion of the C&EI under Missouri Pacific control will thereafter embrace its important line from Chicago to St. Louis and to the important by-pass route to the Southwest via Thebes in southern Illinois.

MoPac also during the year became a joint owner, with the Chicago and North Western Railroad, of the



Alton & Southern Railway, an important switching line at the St. Louis Gateway. It is expected that this acquisition will improve service at that vital gateway and enable the carriers to better their competitive service. Like the C&EI, this property has a great deal of deferred maintenance and needs many capital improvements. It will take another year to put the property in such condition that service will be good and financial results will be satisfactory.

The suit in the New York City Federal Court, brought by MoPac Class B stockholders seeking higher dividends on that stock, is still pending and it is anticipated that it will be some time before it can be reached for trial. The Company is vigorously defending the same.

MoPac continued its opposition to the proceedings by various other western railroads to dismember the Rock Island Railroad, which seriously threaten this company's competitive position; that case is now being briefed and submitted to ICC's Examiners. MoPac also inaugurated opposition to a proposed merger of the Illinois Central and the Gulf, Mobile and Ohio Railroads which the Company feels involves dangerous threat to it in the emerging western railroad merger picture. MoPac's opposition is particularly focused upon the inter-related and alleged control of Illinois Central by Union Pacific Railroad which MoPac seeks to have the ICC investigate.

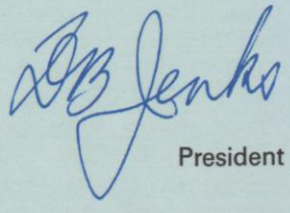
The efforts of the Arkansas railroads to have that state's so-called full crew laws declared unconstitutional again met with failure before the Supreme Court of the United States. Our efforts to be relieved of this unconscionable burden will, however, be continued in other areas because the Company feels that no competitive industry can justifiably be burdened with such extravagant make-work costs, which for the Arkansas operations of MoPac alone amount to over $3,500,000 a year.

Freight Rates

On February 15, 1968, the ICC gave final approval to the railroads' general freight rate increase in Ex Parte No. 256, and on March 7, 1968, the railroads again sought permission to increase their freight rates and charges to partially offset spiraling operating costs experienced since their 1967 proposal and anticipated in the near future. In Ex Parte No. 259, interim increases of no more than 3% were initially permitted on June 19, 1968, but, in November, the suspension of the railroads' original proposal (increases of from 3 to 10 per cent) was largely vacated thereby permitting almost all of the increases to become effective. That decision was confirmed by the Commission's final report of January 23, 1969. However, court litigation concerning the proceeding still continues.

Such increased revenues, of course, are not reflected in their entirety in 1968 accounts because the Ex Parte No. 259 increases were in effect for only part of the year. More significant, it is not anticipated that either Ex Parte No. 256 or Ex Parte No. 259 will improve net income in the future as they were defensive in nature; that is to say, they merely offset, and then only in part, increases in wage rates and other operating expenses already experienced. The Commission estimated that the railroads' increases in operating expenses, rents, taxes (excluding federal income taxes) and fixed charges, which the two general increase proposals were designed to meet, amount to substantially more than the increases in freight rates and charges authorized. Nor did its estimates take into account the time lag for effecting increases on intrastate traffic or increased expenses which will accrue in 1969.

St. Louis, Mo.
March 3, 1969



President

Consolidated Source And Use Of Funds
(In Thousands of Dollars)

	1968	1967
Source of Funds:		
Operations —		
Net income (including extraordinary items)	$ 22,359	$ 31,481
Depreciation and retirements (charges against income not requiring use of funds)	35,915	32,551
Salvage from property sold or retired	6,743	10,441
Proceeds from equipment obligations issued	31,194	35,141
Sale of Santa Fe Industries, Inc. Debentures	8,851	
	105,062	109,614
Use of Funds:		
Property additions	59,921	66,579
Capital fund deposits (for equipment acquisitions)	6,450	
Repayments of equipment obligations	22,614	20,274
Dividends	9,501	9,482
Purchase of securities	13,887	7,730
Other — Net	1,504	(2,417)
	113,877	101,648
Increase (or Decrease) in Working Capital	$ (8,815)	$ 7,966

See Notes to Financial Statements, Pages 12 and 13

Independent Accountants' Opinion

PRICE WATERHOUSE & CO.
ONE MEMORIAL DRIVE
ST. LOUIS 63102

February 21, 1969

To the Stockholders and Board of Directors of
MISSOURI PACIFIC RAILROAD COMPANY

We have examined the consolidated balance sheet of the Missouri Pacific Railroad Company and its subsidiaries as of December 31, 1968 and the related statements of consolidated income, retained income, and source and use of funds for the year. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, except that provision has not been made for deferred federal income taxes as set forth in the supplementary income information, the accompanying consolidated financial statements examined by us present fairly the financial position of the Missouri Pacific Railroad Company and its subsidiaries at December 31, 1968, the results of their operations and the supplementary information on funds for the year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year, except for the change in accounting for certain interline freight revenue as described in Note 3 to the financial statements.

Our opinion dated February 23, 1968 on the 1967 consolidated financial statements examined by us also is subject to the accuracy of the amount estimated for additional transcontinental freight revenue and interest receivable (see Note 4 to the financial statements).

Price Waterhouse & Co.

Missouri Pa

Consolidated

(*In Thousan*

Assets	Dec. 31, 1968	Dec. 31, 1967
Current Assets:		
Cash	$ 25,112	$ 27,344
Temporary Cash Investments, at cost (approximates market)	14,749	30,916
Deposits for Interest and Dividends	8,824	9,036
Accounts Receivable	48,383	38,885
Material and Supplies	13,376	12,133
Other Current Assets	2,279	1,930
	112,723	120,244
Properties: (Note 6)		
Road	814,571	806,619
Equipment	723,367	696,824
Miscellaneous	33,474	37,090
	1,571,412	1,540,533
Accumulated Depreciation		
Road	Cr 105,606	Cr 103,598
Equipment	Cr 279,634	Cr 266,890
Miscellaneous	Cr 10,109	Cr 10,733
Excess of Net Assets (at acquisition) of Consolidated Subsidiaries over carrying value of investments	Cr 39,389	Cr 39,237
	1,136,674	1,120,075
Other Assets and Deferred Charges:		
Investment in Santa Fe Industries, Inc. 6¼% Convertible Subordinated Debentures	24,813	33,664
Investment in Terminal and Other Companies	34,426	24,437
Capital, Insurance and Other Funds	7,188	792
Other	5,167	5,942
	71,594	64,835
	$1,320,991	$1,305,154

ific System

Balance Sheet

of Dollars)

Liabilities	Dec. 31, 1968	Dec. 31, 1967
Current Liabilities: (Exclusive of Long Term Debt Due Within One Year)		
Accounts and Wages Payable	$ 46,605	$ 43,231
Interest and Dividends Payable	7,340	7,697
Unmatured Interest Accrued	13,058	12,959
Federal Income Taxes Accrued (Note 2)	3,395	6,649
Other Taxes Accrued	8,125	7,972
Other Current Liabilities	7,511	6,232
	86,034	84,740
Long Term Debt — Due Within One Year (Equipment Obligations)	22,462	21,378
Long Term Debt (Page 11)	694,990	693,056
Other Liabilities and Deferred Credits	15,376	18,208
Equity of Minority Stockholders in Consolidated Subsidiaries	16,470	16,700
Stockholders' Equity: (Notes 7, 8, 9 and 10)		
Capital Stock — No Par Value		
Class A — Authorized 3,000,000 shares; outstanding 1,861,577 and 1,858,777 shares, respectively (excluding 17,600 shares held by Company)	186,158	185,878
Class B — Authorized 1,000,000 shares; outstanding 39,731 shares	3,973	3,973
Capital Surplus	1,993	544
Retained Income (Page 11)	293,535	280,677
	485,659	471,072
	$1,320,991	$1,305,154
Contingent Liabilities:		
Guarantees of principal and interest with other railroads of obligations of various affiliated companies and of a service interruption policy.		

See Notes to Financial Statements, Pages 12 and 13

Missouri Pacific System

Statement of Consolidated Income

(In Thousands of Dollars)

	1968	1967
Operating Revenues:		
Freight	$413,826	$386,359
Passenger, Mail and Express	14,447	19,810
Switching and Other	17,476	18,023
Total Operating Revenues	445,749	424,192
Operating Expenses: (Note 5)		
Maintenance of Way and Structures (Note 6)	66,802	55,266
Maintenance of Equipment	83,449	80,757
Traffic	11,792	11,435
Transportation	167,193	157,513
General and Miscellaneous	21,376	20,779
Total Operating Expenses	350,612	325,750
Net Revenue from Operations	95,137	98,442
Other Operating Charges:		
Taxes (Except Federal Income Taxes)	32,585	31,103
Equipment and Joint Facility Rents	19,863	15,536
Total Other Operating Charges	52,448	46,639
Net Operating Income (Before Federal Income Taxes)	42,689	51,803
Other Income (Net)	10,919	7,640
Income Available For Fixed Charges (Before Federal Income Taxes)	53,608	59,443
Interest:		
Fixed	22,927	21,771
Contingent	10,184	10,536
Total Interest	33,111	32,307
	20,497	27,136
Federal Income Taxes (Note 2)	430	3,068
	20,067	24,068
Less — Income Applicable to Minority Interests	649	787
Net Income Before Extraordinary Items	19,418	23,281
Extraordinary Items:		
Interline Freight Revenue Accrual (Note 3)	2,941	
Transcontinental Divisions Case Settlement (Note 4)		8,200
Net Income (Including Extraordinary Items) (In Conformity with I.C.C. Accounting Principles — Note 2)	$ 22,359	$ 31,481

Supplementary Income Information

Net Income Before Extraordinary Items as above (In Conformity with I.C.C. Accounting Principles)	$ 19,418	$ 23,281
Adjustments to Generally Accepted Accounting Principles (Note 2): Add or (Deduct) —		
Deferred Federal Income Taxes	(7,971)	(6,427)
Portion of Deferred Federal Income Taxes Applicable to Minority Interests	344	369
Net Income Before Extraordinary Items	11,791	17,223
Extraordinary Items:		
Interline Freight Revenue Accrual (Note 3)	2,941	
Transcontinental Divisions Case Settlement (Note 4)		8,200
Net Income (Including Extraordinary Items) (As It Would Be Stated in Conformity With Generally Accepted Accounting Principles)	$ 14,732	$ 25,423
Depreciation and Retirement Charges Included Above (Note 6)	$ 35,915	$ 32,551

See Notes to Financial Statements, Pages 12 and 13

Missouri Pacific System

Consolidated Retained Income

(In Thousands of Dollars)

	1968	1967
Balance at beginning of year	$280,677	$258,678
Add — Net income (Including Extraordinary Items) (In Conformity with I.C.C. Accounting Principles)	22,359	31,481
	303,036	290,159
Deduct — Cash Dividends —		
Class A Stock — $5.00 per share	9,302	9,283
Class B Stock — $5.00 per share	199	199
Balance at end of year (including $69,927 and $66,185 respectively, appropriated by the Board of Directors) (Notes 7 and 10)	$293,535	$280,677

See Notes to Financial Statements, Pages 12 and 13.

Long Term Debt

(Including Maturities in 1969)

(In Thousands of Dollars)

	Interest Rate	Date of Maturity	Changes 1968 Issued	Changes 1968 Reacquired	Outstanding December 31, 1968 (excluding amounts held by Company)
Missouri Pacific Railroad Company					
First Mortgage Bonds (1)	4¼%	1990 & 2005		$ 4,696	$251,522
General Mortgage Bonds (1)	4¾% (2)	2020 & 2030			116,540
Income Debentures	5% (2)	2045			100,016
Equipment Obligations	2¾% to 6½%	1969 to 1983	$16,725	11,517	83,880
Texas and Pacific Railway Company					
First Mortgage Bonds	5%	2000			18,961
Second Mortgage Bonds	5%	2000			73
General & Refunding Mortgage Bonds (1)	3⅞%	1985		584	21,233
Equipment Obligations	3⅞% to 6¼%	1969 to 1983	10,369	4,817	56,820
Other Majority Owned Subsidiaries	3⅝% to 6¼%	1969 to 1983	4,100	6,562	68,407
Grand Total			$31,194	$28,176	$717,452

Equipment Obligations maturing during each of the next five years	1969	1970	1971	1972	1973
	$22,462	$20,899	$19,874	$19,025	$17,908

(1) Have annual sinking fund requirements.

(2) Contingent interest.

Missouri Pacific System

Notes to Financial Statements

NOTE 1 – PRINCIPLES OF CONSOLIDATION:

The accompanying consolidated financial statements of the Missouri Pacific System include the accounts of the Missouri Pacific Railroad Company and its majority-owned subsidiaries, principally the Texas and Pacific Railway Company which is 95.6% owned. The investment in the Chicago & Eastern Illinois Railroad Company, which was 45.2% owned at December 31, 1968, has not been consolidated and is included in the consolidated financial statements at cost.

NOTE 2 – FEDERAL INCOME TAXES:

The Company and its railroad subsidiaries maintain their books of account, and the accompanying statements have been prepared, in conformity with principles and methods of accounting prescribed or authorized by the Interstate Commerce Commission. These principles and methods do not require provision for deferred federal income taxes as is required under generally accepted accounting principles.

The supplementary income information shown below the statement of consolidated income reflects the adjustments necessary to present net income in conformity with generally accepted accounting principles. The adjustments for deferred federal income taxes provide for the tax effects of all material timing differences (transactions which enter into the determination of pretax accounting income in one year and of taxable income in a different year) in accordance with Opinion 11 of the Accounting Principles Board, American Institute of Certified Public Accountants, which became effective in 1968. The 1967 adjustment has been restated from the amount previously reported which was limited to the tax effect of the excess of tax amortization, accelerated and guideline depreciation over the related book depreciation. As a result of the change in the method of computing deferred federal income taxes, net income in conformity with generally accepted accounting principles has been increased by $1,328,000 from that which would otherwise have been reported for 1968 and by $843,000 from the amount previously reported for 1967. The adjustments necessary to reflect the income tax effects of cumulative timing differences and present the accompanying consolidated balance sheet in conformity with generally accepted accounting principles at December 31, 1968 would result in an increase in current assets of $6,200,000, a decrease in current liabilities of $3,700,000, an increase in other liabilities and deferred credits of $117,400,000, a decrease in equity of minority stockholders of $4,300,000, and a decrease in retained income of $103,200,000.

Investment tax credits applied in reduction of the provisions for current federal income taxes represent the estimated amounts currently realizable and amounted to $1,240,000 and $3,700,000, for 1968 and 1967, respectively. At December 31, 1968, unused investment tax credit carryovers of approximately $18,600,000 are available to offset future years federal income taxes. Of the $18,600,000 carryover, $3,300,000 will expire in 1969, $3,100,000 in 1970, $2,900,000 in 1971, $3,500,000 in 1972, $2,500,000 in 1973, $800,000 in 1974, and $2,500,000 in 1975, if not used.

NOTE 3 – INTERLINE FREIGHT REVENUE ACCRUAL:

At the direction of the Interstate Commerce Commission, certain interline freight revenue has been accrued for the first time during 1968. This accrual comprises an estimate of revenue earned on the railroad companies' traffic which had been delivered off their lines but which had not reached its destination by the end of the period. Prior to 1968, this revenue was included in the period in which the traffic reached its destination and settlement was made by the destination road. As a result of this change, the 1968 Statement of Consolidated Income includes additional freight revenue of $4,762,000 ($3,505,000 after federal income taxes) representing an estimate of the amount of this revenue earned as of the end of the year. Of this amount, $3,996,000 ($2,941,000 after federal income taxes), representing an estimate of the unaccrued amount of this revenue as of the beginning of the year, has been reported as an extraordinary item.

NOTE 4 – TRANSCONTINENTAL DIVISIONS CASE:

During 1967 the Transcontinental Divisions case was resolved by the Supreme Court of the United States upholding the Interstate Commerce Commission's award of an increased share of Mountain Pacific freight revenue to the Midwestern roads. Current settlements under the new divisions were effective January 1, 1968. The amount of the adjustment since July 1, 1963 is expected to be determined finally during 1969 from statistical sampling studies conducted by experts engaged by the parties. The 1967 consolidated financial statements include $14,500,000 ($10,800,000 after federal income taxes) for the estimated additional transcontinental freight revenue and interest receivable of which $11,000,000 ($8,200,000 after federal income taxes) has been reported as an extraordinary item. It is presently contemplated that, when the amount is finally determined, any material adjustment of the estimated amount will be treated as a restatement of 1967 rather than as an adjustment of current earnings for purposes of reporting in conformity with generally accepted accounting principles.

NOTE 5 – RETIREMENT PLAN:

The companies have an unfunded noncontributory pension plan for executives, officials, and certain key employees. Related charges to operating expense in 1968 and 1967 were approximately $2,201,000 and $2,050,000, respectively, representing accruals which include normal cost and amortization of prior service cost over a period of 35 years, plus interest on the recorded unfunded pension liability.

The actuarially computed value of benefits pertaining to retired employees exceeds the recorded pension plan liability by approximately $14,200,000 at December 31, 1968.

NOTE 6 – PROPERTIES:

Properties are stated at estimated original cost as determined by Interstate Commerce Commission valuations (as of January 1, 1955, date of reorganization, as to the parent company and about 1916 as to the subsidiaries) plus additions and betterments at cost and less retirements since the dates of valuations.

The companies follow the straight-line method of depreciation, using various group rates prescribed by the Interstate Commerce Commission, with respect to equipment and depreciable road properties. However, for rails, ties and other track materials, instead of depreciation accounting, they follow an acceptable alternate practice of "replacement" accounting. Under this method replacements in kind are charged to expense while additions and betterments (improvements) are capitalized. The amounts capitalized are not depreciated and are charged against income only when the related properties are abandoned.

At December 31, 1968 consolidated nondepreciable properties, including land and land rights, were approximately $522,000,000.

NOTE 7 – CAPITAL STOCK AND RETAINED INCOME:

As of December 31, 1968, the Company had outstanding 1,901,308 shares of Capital Stock divided into two classes. Of this total 97.9%, or 1,861,577 shares, were Class A Stock and 2.1% or 39,731 shares were Class B Stock. These shares are without par value, but each has a stated value of $100 per share. Holders of Class A and Class B Stock have full voting rights equal to one vote for each share held, but the Class A and Class B shares are entitled to vote separately as a class upon certain matters, including the issuance of additional shares and modifications of present shares.

Dividends on the Class A Stock are non-cumulative and may not exceed $5 per share in any given calendar year. After dividends of $5 per share have been paid on the Class A Stock in any year, dividends may be paid on the Class B Stock in such amount as the Board of Directors may declare. Dividends on both classes of stock are subject to the setting aside of such reserves and making such other provisions as the Board may deem necessary or advisable for working capital or expansion of the business of the Company, including the acquisition of property, or for other corporate purposes. Undistributed earnings of prior years may be used to pay cash dividends in succeeding years on either class of stock.

In the event of liquidation of the Company the holders of Class A Stock shall be entitled to receive out of the assets the maximum of $100 per share before any distribution is made to the holders of the Class B Stock. Thereafter, the holders of the Class B Stock shall be entitled to receive any further distributions out of the assets of the Company without participation by the Class A holders. Neither the Class A nor Class B Stock is convertible into the other class and neither is subject to redemption.

The provisions of the mortgages and indenture relative to priority of call in each year upon "Available Net Income" (as defined therein) have been satisfied and no restriction on the parent company's retained income at December 31, 1968 exists.

NOTE 8 – STOCK OPTION PLAN:

A Restricted Stock Option Plan reserving 100,000 shares of Class A Stock was approved by the stockholders on May 9, 1961. Under the plan, options granted prior to 1964 are cumulatively exercisable to the extent of 25% in each of the third through sixth years and expire ten years after the date of grant. Options granted in 1964 and subsequent are cumulatively exercisable to the extent of 35% in each of the third and fourth years and 30% in the fifth year and expire five years after the date of grant. No additional options can be granted under the plan. A summary of changes in stock options for the year follows:

	Under Option		*Exercisable*	
	Shares	*Price Range*	*Shares*	*Price Range*
Balance, Jan. 1, 1968	22,425	$44.87-92.50	8,425	$44.87-80.37
Options —				
Became exercisable			7,500	59.87-92.50
Exercised	(2,800)	44.87-60.37	(2,800)	44.87-60.37
Balance, Dec. 31, 1968	19,625	44.87-92.50	13,125	44.87-92.50

The aggregate option price of shares under option at December 31, 1968 was $1,580,000.

For the options exercised in 1968, Class A Stock was credited at $100 per share, an aggregate of $280,000, and the difference between the $100 and the option price was charged to capital surplus, an aggregate of $116,000.

NOTE 9 – CAPITAL SURPLUS:

The March 1, 1956 Consummation Order and the Final Decree of the United States District Court for the Eastern District of Missouri, approving the reorganization of the Missouri Pacific Railroad Company, provided that the rights of holders to surrender old securities of the Company and receive cash therefor would terminate on March 1, 1968, that the Company should eliminate the unused reserve therefor, and that all cash not distributed would become the sole and exclusive property of the Company, free and clear of any right, title and interest other than that of the Company. Accordingly, the remaining balance in the Company's reserve for old securities not surrendered was eliminated as of that date. The elimination of this reserve is reflected in the 1968 consolidated financial statements by an increase in capital surplus of $1,565,000, and an increase in current earnings of $565,000. There was no estimated income tax effect involved.

NOTE 10 – LEGAL PROCEEDING:

The lawsuit in the New York City Federal Court, brought by the Company's Class B stockholders against the Company and its directors and Mississippi River Corporation, is still pending and it is anticipated that it will be some time before it can be reached for trial. These stockholders, who sue on behalf of all the Class, assert that the dividends paid on the Class B Stock are inadequate and that Mississippi River Corporation is seeking to enrich itself by depriving those stockholders of their share of the Company's earnings. The Courts are asked to order Missouri Pacific and its directors to declare dividends on the Class B Stock in such amounts as the Court shall determine to be just and reasonable out of retained income for the years 1955 through 1967, plus interest thereon, and that defendants be required to pay adequate dividends in the future. It is the position of the Company that the suit is without foundation and it is vigorously defending the same.

Computation And Application Of Available Net Income

Income of Missouri Pacific Railroad Company and Its Wholly-Owned Railway Companies (as required by the Company's Mortgages and Indenture)

(In Thousands of Dollars)

	1968	1967
Income before Fixed Charges and after Federal Income Taxes	$41,761	$57,723
Income of Wholly-Owned Railway Companies	265	242
Road Property Retired and Charged to Operating Expenses	2,250	68
	44,276	58,033
Less — Dividends of 100% Railway Companies included in Missouri Pacific Income	450	200
Total Income Available for Fixed Charges	43,826	57,833
Fixed Charges	14,718	14,714
Available Income	29,108	43,119
Capital Expenditures Fund	3,859	3,631
Remaining Available Income	25,249	39,488
First Mortgage Sinking Fund	771	771
Remaining Income	24,478	38,717
Interest on General Mortgage Bonds, Series A	2,709	2,832
Remaining Income	21,769	35,885
Sinking Fund on General Mortgage Bonds, Series A	350	350
Remaining Income	21,419	35,535
Interest on General Mortgage Bonds, Series B	2,559	2,703
Remaining Income	18,860	32,832
Sinking Fund on General Mortgage Bonds, Series B	338	338
Remaining Income	18,522	32,494
Interest on Income Debentures	4,916	5,001
Balance	$13,606	$27,493

Missouri Pacific Railroad Company

Statement of Income (Corporate)

(In Thousands of Dollars)

	1968	1967
Operating Revenues:		
Freight	$307,674	$289,320
Passenger, Mail and Express	9,980	14,740
Switching and Other	13,877	14,269
Total Operating Revenues	331,531	318,329
Operating Expenses:		
Maintenance of Way and Structures	52,697	43,205
Maintenance of Equipment	54,903	53,197
Traffic	8,031	7,750
Transportation	117,896	111,783
General and Miscellaneous	16,343	15,809
Total Operating Expenses	249,870	231,744
Net Revenue from Operations	81,661	86,585
Other Operating Charges:		
Taxes (Except Federal Income Taxes)	24,105	22,995
Equipment and Joint Facility Rents	32,053	27,372
Total Other Operating Charges	56,158	50,367
Net Operating Income (Before Federal Income Taxes)	25,503	36,218
Other Income (Net):		
Intercompany Dividends (Eliminated in Consolidation)	5,739	9,810
Other, Net	8,252	5,064
Total Other Income	13,991	14,874
Income Available For Fixed Charges (Before Federal Income Taxes)	39,494	51,092
Interest:		
Fixed	14,718	14,714
Contingent	10,184	10,536
Total Interest	24,902	25,250
	14,592	25,842
Federal Income Taxes	Cr 65	2,569
Net Income Before Extraordinary Items	14,657	23,273
Extraordinary Items:		
Interline Freight Revenue Accrual	2,202	
Transcontinental Divisions Case Settlement		9,200
Net Income (Including Extraordinary Items) (In Conformity with I.C.C. Accounting Principles)	$ 16,859	$ 32,473

Supplementary Income Information

Net Income Before Extraordinary Items as above (In Conformity with I.C.C. Accounting Principles)	$ 14,657	$ 23,273
Adjustments to Generally Accepted Accounting Principles — Deferred Federal Income Taxes	(3,007)	(2,000)
Net Income Before Extraordinary Items	11,650	21,273
Extraordinary Items:		
Interline Freight Revenue Accrual	2,202	
Transcontinental Divisions Case Settlement		9,200
Net Income (Including Extraordinary Items) (As It Would be Stated in Conformity With Generally Accepted Accounting Principles)	$ 13,852	$ 30,473
Depreciation and Retirement Charges Included Above	$ 21,486	$ 19,365

Texas and Pacific System

(Owned 95.6% By Missouri Pacific Railroad Company)

Statement of Consolidated Income

(In Thousands of Dollars)

	1968	1967
Operating Revenues:		
Freight	$ 86,825	$ 79,385
Passenger, Mail and Express	4,467	5,070
Switching and Other	2,660	2,775
Total Operating Revenues	93,952	87,230
Operating Expenses:		
Maintenance of Way and Structures	12,579	10,892
Maintenance of Equipment	17,349	16,174
Traffic	3,255	3,124
Transportation	38,858	35,958
General and Miscellaneous	4,166	4,102
Total Operating Expenses	76,207	70,250
Net Revenue from Operations	17,745	16,980
Other Operating Charges:		
Taxes (Except Federal Income Taxes)	6,058	5,695
Equipment and Joint Facility Rents	2,946	3,610
Total Other Operating Charges	9,004	9,305
Net Operating Income (Before Federal Income Taxes)	8,741	7,675
Other Income (Net)	1,693	1,860
Income Available For Fixed Charges (Before Federal Income Taxes)	10,434	9,535
Fixed Interest	5,580	4,662
	4,854	4,873
Federal Income Taxes	Cr 364	Cr 156
	5,218	5,029
Add-Loss Applicable to Minority Interests	44	8
Net Income Before Extraordinary Item	5,262	5,037
Interline Freight Revenue Accrual	739	
Net Income (Including Extraordinary Item) (In Conformity with I.C.C. Accounting Principles)	$ 6,001	$ 5,037

Supplementary Income Information

Net Income Before Extraordinary Item as above (In Conformity with I.C.C. Accounting Principles)	$ 5,262	$ 5,037
Adjustments to Generally Accepted Accounting Principles — Deferred Federal Income Taxes	(3,126)	(2,381)
Net Income Before Extraordinary Item	2,136	2,656
Interline Freight Revenue Accrual	739	
Net Income (Including Extraordinary Item) (As It Would Be Stated In Conformity With Generally Accepted Accounting Principles)	$ 2,875	$ 2,656
Depreciation and Retirement Charges Included Above	$ 7,992	$ 6,919

Chicago & Eastern Illinois System

(Owned 45.2% By Missouri Pacific Railroad Company)

Statement of Consolidated Income

(In Thousands of Dollars)

	1968	1967
Operating Revenues:		
Freight	$ 44,925	$ 38,698
Passenger, Mail and Express	1,187	2,168
Switching and Other	3,665	3,226
Total Operating Revenues	49,777	44,092
Operating Expenses:		
Maintenance of Way and Structures	8,287	8,525
Maintenance of Equipment	9,106	8,426
Traffic	1,632	1,609
Transportation	18,110	17,140
General and Miscellaneous	2,960	3,015
Total Operating Expenses	40,095	38,715
Net Revenue from Operations	9,682	5,377
Other Operating Charges:		
Taxes (Except Federal Income Taxes)	3,376	3,188
Equipment and Joint Facility Rents	5,179	3,157
Total Other Operating Charges	8,555	6,345
Net Operating Income (Loss) (Before Federal Income Taxes)	1,127	(968)
Other Income (Net)	275	154
Income (Loss) Available for Fixed Charges (Before Federal Income Taxes)	1,402	(814)
Fixed Interest	2,089	2,239
	(687)	(3,053)
Federal Income Tax Refund	99	
Net Loss (In Conformity with I.C.C. Accounting Principles)	$ (588)	$ (3,053)

Supplementary Income Information

Net Loss as above (In Conformity with I.C.C. Accounting Principles)	$ (588)	$ (3,053)
Adjustments to Generally Accepted Accounting Principles — Deferred Federal Income Taxes	330	1,491
Net Loss (As It Would Be Stated In Conformity With Generally Accepted Accounting Principles)	$ (258)	$ (1,562)
Depreciation and Retirement Charges Included Above	$ 3,067	$ 3,473

THE TRUCK-RAIL NETWORK OF THE SYSTEM LINES

The Missouri Pacific—Texas & Pacific System totals 11,463 miles of railroad in an area extending from the Mississippi River on the east, to the Colorado Rockies, from Omaha and St. Louis on the north, to the Gulf of Mexico and the Rio Grande.

Its on-line territory, in which traffic originates and terminates, includes 12 states in the midwest, south and southwest. With gateways to and from the west at Pueblo and El Paso, and to the east at St. Louis, Memphis and New Orleans, the MP—T&P combination provides an exceptionally wide choice of routes for overhead east-west traffic. Handling substantial volumes of export-import traffic through 12 Gulf ports and through the Brownsville, Laredo and El Paso gateways to Mexico, it is an important link in foreign commerce as well as one of the nation's major domestic carriers.

Supplementing the rail lines is a network of some 16,800 miles of truck routes operated by Missouri Pacific Truck Lines, Inc., and the Texas & Pacific Motor Transport Company. Much of the highway mileage parallels the rail lines but many routes provide scheduled freight service to places not reached by the railroads. The two highway subsidiaries also perform all the terminal and piggyback ramp loading and unloading for Missouri Pacific Railroad—Texas & Pacific Railway billed traffic and over-the-highway service for piggyback traffic.

Office of the Secretary
MISSOURI PACIFIC RAILROAD CO.
2206 Missouri Pacific Bldg.
210 N. 13th St., St. Louis, Mo. 63103

MISSOURI PACIFIC RAILROAD ANNUAL REPORT 1968